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EUROPEAN COMMUNITIES: The decline in value of the European joint float currencies has halted temporarily, but internal pressures may threaten the structure of the float itself.

At this week's central bankers' meeting in Basel, there was serious disagreement on the management of the float's rate relative to the dollar. Other EC members refused to join Bonn in intervening to support their currencies against the dollar. The Bundesbank, which is seeking to stem the devaluation of the mark, reportedly has sold over $1 billion since the start of the year. Bonn also is considering relaxation of controls on capital which discourage Germans from borrowing abroad and non-Germans from increasing their holdings of marks. The differing policies among the Europeans drove the mark to the top of the joint float band yesterday while the French franc sank to the bottom.

Bonn will not be willing to draw down sharply its dollar reserves to keep the mark from declining further, but it seems determined to prevent a rapid devaluation. Other joint float members would probably welcome further devaluation of their currencies in order to gain a trade advantage with the US and thus partially offset their skyrocketing oil import bill. Furthermore, these governments would like to avoid heavy dollar sales that would complicate domestic monetary management. Unless these differences are resolved by agreement among the EC countries or at next week's IMF meeting in Rome, the joint float may be in jeopardy. [redacted] 25X1

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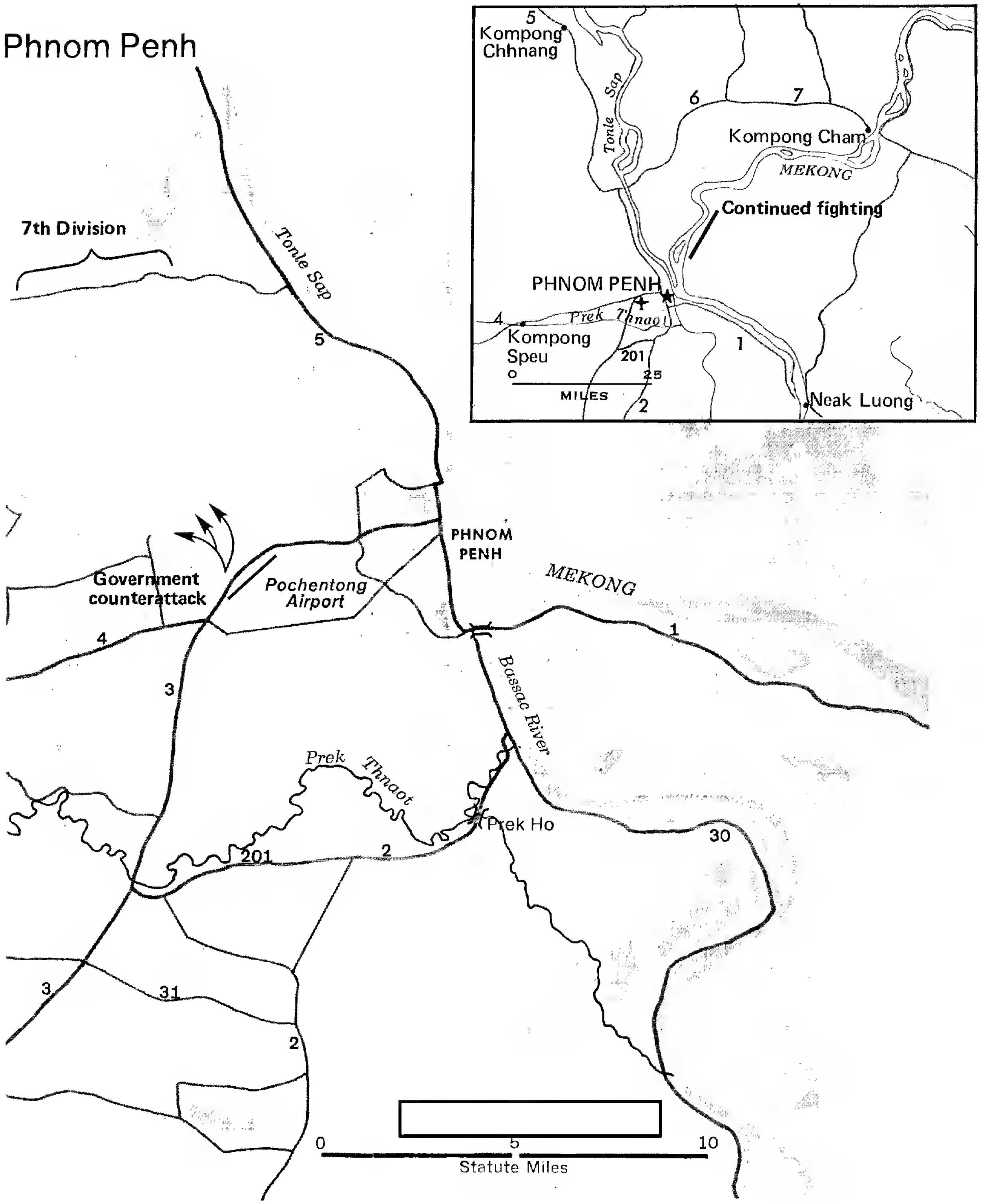

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CAMBODIA: Cambodian Army forces have blunted the initial Khmer Communist drive against the capital's northwestern defenses. Government armor and infantry units, with the army's 1st Division joining the counterattack, are now taking the fight to insurgent units three to five miles northwest of Phnom Penh's airport. The airport is open despite occasional shellings, and Phnom Penh continues to be hit by sporadic rocket fire.

With the government concentrating on defensive efforts northwest of the city, the Communists are now turning their attention to units of the 7th Division strung out along a secondary road west of Route 5. Elements of the 7th have been cut off for several days. [redacted] 25X1

25X1 [redacted] defeat of the 7th, perhaps the army's best division, was a major objective.

Action is lighter on other fronts around the capital, although steady Communist shellings on the Mekong River's east bank are keeping government troops pinned down in riverside villages just upstream from Phnom Penh. [redacted] 25X1

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The isolated provincial capital of Takeo is under increasingly heavy pressure and the government is planning to send in reinforcements. [redacted] 25X1

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[redacted] 25X1

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CUBA: Top Cuban leaders apparently are still opposed to improved relations with the US.

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[redacted] early press accounts of remarks by [redacted] to Mexico at a press conference earlier this week, seemingly indicating a softening in Cuba's attitude toward the US, were overstated. His remarks on this subject showed no significant change from previous statements by top Cuban officials in the past year.

The ambassador's primary purpose in meeting with the press was probably to disparage the significance of the forthcoming meeting in Mexico between Secretary of State Kissinger and the Latin American foreign ministers. The ambassador said that nothing will come of the meeting, because the Latin American governments "lack the political will" to confront the US in a unified manner. The concept of an aggressive and unified Latin America--preferably led by Cuba--has long been advocated by Havana as the only way to obtain concessions from the US. [redacted]

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NATO: Many NATO allies remain opposed to increasing their contributions to joint NATO budgets so the US share may be reduced.

The efforts of Secretary General Luns and the Belgian representative at a session of the North Atlantic Council on January 9 to initiate positive Council action were undercut by the major European allies, who agreed only to refer the question to a committee for consideration. The West German, British, and French representatives restated their long-standing opposition to participating in any multilateral scheme to reduce the balance-of-payments deficit incurred by the US in stationing forces in Europe.

The West Germans have long held that the bilateral offset agreement with the US is the only contribution they can make to resolve the US problem. The British argue that they have a relatively greater balance-of-payments problem than the US and thus cannot participate in the multilateral relief scheme. France refuses to consider any burden-sharing proposals because it is not a member of the NATO integrated military command. Some of the smaller countries also plead that they cannot afford additional defense expenditures.

Some of the smaller states, including Belgium, the Netherlands, and Norway, support the US proposals, but are reluctant to make greater contributions unless all the allies do so.

The US appeal for relief through the burden-sharing proposals has been prejudiced by the recent improvement in the overall US balance-of-payments position. An Italian official argued recently that this factor and the serious fuel situation in Europe have changed the premises on which the US proposals were based. NATO Secretary General Luns alluded to this at the Council meeting, stating that it is possible that the multilateral burden-sharing exercise will be overtaken by economic events. The Belgian

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representative also remarked that if the European economic situation deteriorated enough, the allies might have to ask the US for relief from their military balance-of-payments deficit. [redacted] 25X1

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[redacted] 25X1

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JAPAN: Tokyo is discouraging capital outflows to prevent official foreign exchange reserves from dropping below $10 billion. Government permission will be required by private individuals to purchase US short-term treasury bills, and Japanese security companies are being admonished not to increase holdings of foreign stocks and bonds. Tokyo hopes to avoid broader formal sanctions that would openly conflict with earlier capital liberalization programs.

Japanese purchases of foreign securities totaled about $1.7 billion in 1973; US securities became particularly attractive when it became apparent late in the year that the yen would weaken further. With official reserves down to $12.2 billion at the end of 1973 and still falling, Tokyo is seeking to restrict the bulk of Japanese investment activities abroad to resource development projects. 25X1

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SOUTH KOREA: Opposition groups, although concerned by President Pak's tough emergency measures of January 8, seem determined to continue pressing for government liberalization. Leaders of the opposition New Democratic Party have resolved to challenge the government's move through legal channels, despite the real risk of arrest and imprisonment. The leader of the group of intellectuals who are circulating a reform petition told the US Embassy that his efforts will continue. Christian leaders are planning to consult on their course of action.

The government, meanwhile, is trying to bring the situation under control and to present its case in the best light. It is suppressing press coverage of the few arrests made so far [redacted] 25X1 In public statements and in meetings with diplomats, government spokesmen are stressing that the new measures will apply only to a very small "radical antigovernment" element. For his part, Prime Minister Kim Chong-pil is trying to preserve a continuing dialogue with church and intellectual leaders.

Pak's action this week has almost certainly cost him considerable political capital at home and abroad. A number of middle-level government officials are reported to be dismayed by his actions. [redacted] 25X1 South Korean allies have indicated a belief that Pak's move was unnecessary, and the Japanese ambassador to Seoul privately recommended that his government broaden its contacts to include elements of the political opposition. [redacted] 25X1

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BRAZIL: Real gross national product rose 11.4 percent last year to an estimated $60 billion. The increase, the largest since the 1964 revolution, placed Brazil's economy among the world's fastest growing. Industrial expansion and a strong export drive underlie the advance. Industrial output gained over 16 percent and exports, despite controls on agricultural and steel products, jumped 53 percent to more than $6 billion.

Inflation remains one of Brazil's major economic problems. The wholesale price index last year rose 15.5 percent--lower than previous inflation rates but far above the highly publicized government goal of 12 percent.

Brazilian officials are predicting an 8- to 9-percent growth in this year's real gross national product, despite problems caused by higher oil prices. Brasilia's large foreign exchange reserves--in excess of $6 billion--should enable it to pay for increased oil costs in the short run without undue hardship. Higher oil prices over the long run, however, could restrict growth.

Brazil has succeeded in ensuring sufficient oil supplies from the Arabs and elsewhere and has not yet adopted any restrictive measures on consumption. The government has already absorbed $100 million of higher import prices for oil in order to maintain the selling price for regular gasoline at 62 cents a gallon. [redacted]

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FOR THE RECORD*

<u>Africa - Arab States</u>: The Arab League is arranging a meeting in Cairo on January 22 between a committee of the Organization of African Unity (OAU) and Arab foreign and petroleum ministers to find ways of ensuring an oil supply for black Africa. Plans for setting up an African development fund by the Arabs and for Arab technical assistance for black Africa will also be discussed. The OAU sought the meeting to secure implementation of promises given by the Arabs last November at the Algiers summit, after black Africa sided with the Arabs during the Middle East war by breaking relations with Israel. [redacted]

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This item was prepared by CIA without consultation with the Departments of State and Defense.

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